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SN 131

Use of Reserve of Education Subvention

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Education subvention from the national budget to local budgets as founders of secondary schools is the main budgetary instrument to support local expenditures on secondary education in Ukraine. Since its introduction in 2015, the subvention included a reserve of at most 1% (art. 103-2 of the Budget Code). While the main part of education subvention must be distributed among local governments according to a per student allocation formula, adopted each year through a decree of Cabinet of Ministers of Ukraine (CMU), prepared by the Ministry of Education and Science of Ukraine (MES), the reserve may be allocated based on the needs of territorial gromadas. The allocation is decided by the Cabinet of Ministers of Ukraine (art. 103-2 of the Budget Code). In theory, this means that the reserve is a flexible instrument to implement national policy and to react to unforeseen situations which may arise during the budget year. However, in practice this is a highly inflexible instrument, spent only at the end of the budget year on various investment programs. This unfortunate situation and policy options of how it can be corrected is the focus of the present Short Note 131.

In the first section we review the present regulations of the use of education subvention and we document how they are applied in practice. For completeness, we include a discussion of the funds of education subvention allocated for uncontrolled territories, because they are treated similarly to the reserve. The following section, for comparative purposes, discusses briefly the Polish model of regulating and using the reserve. Section 3 provides a list of possible strategic functions of the

reserve, to strengthen their use as a policy instrument of MES. In the final section we formulate several recommendations.

The present Short Note 131 is continuation of analytical support to the Ministry provided by the Ukrainian-Swedish project “Support to Decentralization in Ukraine” (SDU). Recent short notes on the education subvention include SN 121 on monitoring of the use of education subvention (December 2020), SN 124 on normative class sizes in 2021 (April 2021), SN 125, 126 and 127 on policy options regarding normative class sizes (May 2021). The problems of the reserve of education subvention was also already addressed by SDU experts. In February 2018, short note 89 on this topic was prepared and submitted to the Ministry of Education and Science.

1. Present regulation and practice of the use of the reserve

Education subvention is defined and regulated in art. 103² of the Budget Code, Law № 2456-VI of July 8, 2010 (Бюджетний кодекс України). The introduction of education subvention into Ukrainian law was a part of major reform of 2014 introducing modern public finance rules in Ukraine (Law № 79-VIII of December 28, 2014). Education subvention is a transfer from the national budget to local budget to finance recurrent expenditures on provision of secondary education. Since the beginning of 2017, education subvention may be used exclusively for the salaries of pedagogical staff (Law № 1789-VIII of December 20, 2016).

The budget reform of 2014 introduced also the reserve of the education subvention. The reserve is defined in part 3 of article 103², in the following two clauses:

The content of the education subvention foresees reserve of funds, whose amount cannot exceed 1 percent of the total amount of subvention.

The Cabinet of Ministers of Ukraine executes the allocation of the reserve of education subvention and may determine direction of the use of these funds.

(При цьому у складі зазначеної субвенції передбачається резерв коштів, обсяг якого не може перевищувати 1 відсотка загального обсягу субвенції. Кабінет Міністрів України здійснює розподіл резерву освітньої субвенції та може визначати напрями використання таких коштів.)

It is worth noting that the initial formulation of the last clause was that the use of the reserve requires agreement of the Budget Commission of the Verhovna Rada; in view of some arising tensions this last condition was dropped since the beginning of 2018 (Law № 2233-VIII of December 7, 2017).

Moreover, initially the purpose of the reserve was formulated as:

for expenditures, which could not have been taken into account when applying the formula

(для здійснення видатків, що не могли бути враховані при застосуванні формули)

This is a rather unclear formulation, but presumably it refers to unpredictable situations, like natural disasters or sudden migrations of students. Since 2017, when the education subvention was restricted to the salaries of pedagogical staff, this formulation was dropped. Presently, the specific use of the funds from the reserve is determined every year in the decree of Cabinet of Ministers which defines this allocation (see below).

According to the Budget Code, the reserve of education subvention may, but does not have to, be a part of the yearly budget laws. However, in practice the reserve was introduced every year. The following Table 1 shows the amounts of the education subvention and of the reserve in recent years.

Table 1. Reserve of education subvention 2018-2021

Budget year	Subvention amount (million Hr)	Reserve (million Hr)	Share of subvention
2018	61 712,6	517,3	0,84%
2019	69 623,6	549,6	0,79%
2020	78 503,7	595,2	0,76%
2021	99 647,4	668,4	0,67%

We observe steady decline of the reserve as share of the total subvention amount, from 0,84% down to 0,67%.

Alongside the reserve of education subvention, the public finance system of Ukraine includes a second allocation of education subvention which plays the same role, namely the allocation for territories of Doneck and Lugansk oblasts beyond the effective control of the national government. These funds are not used during the budget year and therefore can be either used for other local governments or remain unused (returned to the national budget). The amounts for uncontrolled territories are listed in the following Table 2.

Table 2. Allocation for uncontrolled territories 2018-2021

Budget year	Allocation for uncontrolled territories (million Hr)	Share of subvention
2018	1 641,0	2,66%
2019	681,0	0,98%
2020		0,00%
2021		0,00%

We note that initially allocation for territories beyond the control of Ukrainian government were quite considerable, significantly higher than the reserve itself. These allocations were reduced in 2019 and discontinued in 2020. The decrease of the share of total funds playing the role of the reserve, namely the reserve and the funds allocation for uncontrolled territories is dramatic, from 3,50% in 2018 to just 0,67% in 2021. This represents major change of education policy, largely unnoticed in Ukraine.

It is important to note that the reserve of education subvention is not stated directly in the yearly budget laws of Ukraine. The allocation of education subvention is provided in an Annex of the budget law (the number of this Annex changes in 2021 it was 6), with an amount for each local budget and with the total amount. The difference between the stated total of subvention and the sum of amounts of subvention for each local budget represents the reserve of education subvention and the allocation for uncontrolled territories. This common treatment implies that the intended use of the reserve and the allocation for uncontrolled territories is the same. For this reason, the amounts provided in Table 1 and Table 2 are not stated in the budget laws, only their sum may be deduced from these laws. The source of data for these two tables is the Ministry of Education and Science (Excel files simulators). Nevertheless, it is important to stress that hiding the reserve in the budget law in this manner is not a good budgeting practice.

The allocation of the reserve of education subvention is made through a Decree of Cabinet of Ministers of Ukraine. The last three decrees are recalled in the following table (the reserve for 2021 is still not allocated).

Table 3. Decrees on the allocation of the reserve 2018-2020

Year	Decree number	Date of issue
2018	№ 1012-p	December 18, 2018
2019	№ 1106-p	November 27, 2019
2020	№ 1570-p	December 16, 2020

We note in Table 3 that these decrees come towards the end of the budget year. If funds from the reserve are allocated in the middle of December, they will reach local budgets in the last days of the year, and therefore will not be used rationally for the salaries of pedagogical staff. These funds will entirely be left over for the next budget year as so called remaining funds (залишки). Every year, the decree defines a specific purpose for the funds from the reserve.

Moreover, these decrees allocate the funds only to the level of oblasts. Further allocation of these funds to local budgets, or in some cases actual spending of these funds, is the responsibility of oblast administrations.

In 2018, the reserve was divided into three parts: for teaching aids in Ukrainian for schools teaching in minority languages (10%), for equipment of laboratories for natural sciences and mathematics (38%), for ensuring proper sanitary conditions in secondary schools (52%). For the second and third part listed here, the decree defined the minimum level of local co-financing, depending on school location.

In 2019, the allocation of the reserve was performed in the same decree as the reallocation of funds for uncontrolled territories (see Table 4). This further strengthens the similarity of these two parts of the education subvention.

In 2019, the combined funds of the reserve and for uncontrolled territories were divided into four separate parts: for school buses (55%), for repair and equipment of canteens (36%), for ensuring proper sanitary conditions in secondary schools (5%), for equipment of special schools (4%). The decree states that further allocation of funds to local governments must be regulated by MES.

In 2020, the whole reserve was destined for purchases of school buses, including buses with places for handicapped students. The conditions for the use of funds, including local co-financing, were specified in the decree. Oblast administration were tasked with spending these funds (together with funds reallocated to them from other budget programs in the same decree) in a centralized manner.

It should be noted that purposes of funds from the reserve of education subvention is in contradiction to the purpose of the subvention, which is only for salaries of pedagogical staff. This budget restriction on the use of funds is avoided because the allocated funds from the reserve are used in the following budget year, as remaining funds (залишки). This arrangement means that the reserve is used as a new grant to local governments to support various education needs, to be used in the following budget year. In this sense it is no longer a real reserve of education subvention.

Similarly to the allocation of the reserve, decrees of the Cabinet of Ministers are used to allocate the unused funds destined for uncontrolled territories. Technically, this is no longer allocation of the reserve (розподіл), but reallocation of education subvention (перерозподіл). The following Table 4

lists the decrees defining such reallocation (there was no reallocation for 2020, because no such funds were allocated, see Table 3).

Table 4. Decrees on reallocation of funds for uncontrolled territories 2018-2019

Year	Decree number	Date of issue
2018	№ 282-p	April 25, 2018
	№ 624-p	September 5, 2018
	№ 965-p	December 12, 2018
2019	№ 1106-p	November 27, 2019

In 2018, three decrees were adopted regarding the use of unspent funds of education subvention for uncontrolled territories, which were equal to 1 641 million (see Table 2). In April, 1 100 million were reallocated to support preparation of cadres by higher education (budget program 2201160). In September, 441 million, together with funds for other budget programs, were reallocated for the same purpose. In December, remaining 100 million, together with funds from other budget programs, were reallocated for the same purpose and, partially, for Small Academy of Sciences (budget program 2201120). It is worth noting that these considerable funds were used for education purposes, but not for secondary education. Effectively, the total amount of education subvention was reduced by 2,6%.

In 2019, there was one decree covering both the funds for uncontrolled territories and the reserve. As already discussed above, the funds were used for 4 investment programs for secondary education.

We conclude by noting that unspent funds for uncontrolled territories, similarly to the reserve of education subvention, are used not as real reserve of the subvention, to support specific needs of local governments during the budget year, but as source of funds for different needs of the education system, mainly for higher education.

2. Polish model of the reserve of education subvention

In the present section we briefly outline the main regulations of the use of the reserve of education subvention in Poland.

The main transfer from the national budget to local budgets to support the financing of primary and secondary schools, as well as a range of non-school educational tasks of local governments, is the educational part of the general subvention, usually called in Poland “education subvention”. Education subvention is a general grant, its funds may be spent on any budget program, not just on education. This subvention is allocated to local governments on the basis of a formula which uses the number of students in different groups as the main factor (the formula is quite complex and includes over 40 coefficients). According to the law, the education subvention must include a reserve equal to 0,4% of the total amount (initially, in 1993, the reserve was much higher at 2%, over time it was reduced step by step to the present value). The amount of the reserve is stated directly in the budget law. The whole reserve must be allocated before end of November, but many specific amounts are used much earlier.

The reserve is allocated to individual local governments by the Ministry of Finance in agreement with the Ministry of National Education. In order to receive the allocation, local governments must submit

applications to the Ministry of National Education. These applications must follow prescribed criteria, format and deadlines for submission, established every year by the Ministry of National Education (discussed below). The allocation for school founders is based on the assessment of their applications. Applications received earlier are assessed higher.

The applications of local governments are first reviewed by a dedicated unit in the Ministry, and then discussed by the appropriate team of Joint Government-Local Government Commission. The Joint Government-Local Government Commission is a high-level public institution composed of representatives of the national government and of national associations of local governments (since 2008 there are 6 such associations). Presently the Joint Commission has 12 members representing the local governments and 12 members representing the Government of Poland, most of them at the level of Deputy Minister. It is co-chaired by two persons, representing both sides. The Joint Commission sets up teams working in different spheres of local government responsibilities (presently there are 12 such teams). Education issues are the competence of the Education, Culture and Sport Team of the Joint Commission. This team is presently composed of 6 representatives of the national government and 19 representatives of local governments and of their associations.

The discussion of the applications for the reserve of education subvention conducted by the Education, Culture and Sport Team result in recommendations, which applications should be funded and to what extent (fully or partially), and which should be rejected. The list of school founders whose applications have been positively assessed by the Team is published by the Ministry (without details and without amounts). The final decision is taken by the Ministry of Finance.

The criteria for allocation of the reserve are published every year by the Ministry of National Education. For each criterion the Ministry also determines the deadline for applications from local governments. The criteria are typically continued from previous years, but may be adjusted. For 2019 the Ministry adopted 9 criteria:

1. Increase of the number of students in September. The additional funding will cover the increased amount of the education subvention, based on the allocation formula. The deadline for applications is October 15.
2. Fire or similar damages to school buildings. The additional funding will be no more than 50% of the documented costs of repair. The deadline for applications is October 8.
3. Damages to school buildings dues to natural disasters (flooding, earthquakes, hurricanes). The additional funding will cover repair costs minus insurance received by the school founder. The deadline for applications is October 29.
4. Expenditures for severance payments for redundant teachers. The additional funding will cover the costs of paying teachers who lost work due to school closure their severance payments. The deadline for applications is September 24.
5. Teaching aids for natural sciences in primary schools. This criterion was introduced for years 2018 to 2021. The additional funding will cover the costs of new equipment bought by the school founder, documented in invoices, on condition that the school did not benefit from this support in previous years. The deadline for the applications is May 31.
6. Teaching equipment in newly opened classrooms or for teaching new professions. The additional funding will cover the costs of new equipment, documented in invoices. The deadlines for applications are May 28 for classrooms opened for the previous budget year and October 4 for classrooms opened during the current budget year.

7. Activities to strengthen the knowledge of pupils. The additional financing will cover the costs of in-person additional teaching activities, organized to counter the negative effects of distant learning. New legal acts were adopted to define and regulate these activities. The reserve of education subvention for 2021 was specially increased for this purpose. No deadlines for applications are set.
8. Correction of data errors in statistical reporting. The additional funding will cover the increased amount of the subvention according to the formula, if the errors were caused by the aggregation of data by the Ministry. The deadline for applications is May 28.
9. Events of unique character not foreseen by other points. The additional funding will depend on the nature of the unique event. The deadline for applications is September 15.

The criteria may change from year to year. For example, in the above list criterion 7 was introduced in 2021 for the first time, due to pandemic.

For each criterion, together with the deadlines listed above, the Ministry defines the format of the application and the scope of data which must be provided together with the submission.

To conclude, we summarize the main differences between the Ukrainian and the Polish model:

- Purpose of the reserve. Polish model, unlike the Ukrainian model, defines specific criteria for which the reserve may be used before decisions on their basis are taken. These criteria clarify for all stakeholders what is the purpose of the reserve. To ensure the flexibility of the system, the criteria are adjusted every year.
- Responsiveness to needs. Polish model, unlike the Ukrainian model, allocates funds from the reserve in response to applications submitted by local governments (with additional required information). The needs of applicants as stated in their applications are assessed and compared by the team including many representatives of local governments, not just government officials.
- Transparency of the procedure. Polish model, unlike the Ukrainian model, includes procedures for public discussions. The allocation is determined in dialogue with representatives of associations of local governments, meaning that decisions of the national government are well known and understood by all stakeholders.
- Schedule of allocation. Polish model, unlike the Ukrainian model, includes clear deadlines for the use of the reserve. For each criterion, specific deadlines are defined. In this way, actual needs of the local governments during the current budget year may be met.
- Consistency of the subvention and the reserve. Polish model, unlike the Ukrainian model, allows the use of the funds from the reserve for specific education needs, for which also the funds from the subvention may be used.

3. Strategic role of the reserve

In the present section, we propose the formulation of specific uses of the reserve of education subvention in Ukraine during the budget year. Our approach is based on the experience of Poland (see the previous section), but with an important difference.

The reserve of the education subvention in Ukraine should be used for the same purpose as the subvention itself. Until 2017, during the budget year the reserve could have been used, like the subvention, to support local governments in any emergencies, such as fire, very hard winter, or

sudden influx of students from other territories of the country, and for any type of investments, like busses or school laboratories. Since 2017, the purpose of the education subvention is financing the salaries of pedagogical staff. The same applies to the use of the reserve during the budget year.

This legal restriction must be observed when valid and important uses of the reserve of education subvention are proposed. We can propose several such uses of the reserve:

1. Problems created by incomplete or mistaken statistical data.

Education statistical data in Ukraine remain to be weak, despite recent progress achieved through the implementation of electronic EMIS-type system DISO. This is in part due to the lack of a functional registry of secondary schools, which makes control of submission of statistical reports ZNZ-1 rather difficult. There are also inconsistencies of how various data is reported (for example schools report separately students in satellite schools, and also these students together with the students of central schools, which is not consistently interpreted). Problems due to errors in statistical data, if identified as such by the Ministry, may be corrected by allocation of additional funds from the reserve.

2. Problems created by an increase of the number of students in September.

Typically, the number of students change in September, in the middle of the school year. This may lead to an increase of the number of classes, and hence to higher than anticipated costs of salaries of pedagogical staff. In some case, the increase may be high enough to create budgetary problems for the school founder (including the need to rebalance the local budget). If properly documented by the local government, these specific problems may be resolved by allocation of additional funds from the reserve.

3. Problems created by weaknesses of the allocation formula.

The allocation formula for education subvention is based on the concept of normative class size, assigned to each local government on the basis of objective criteria, namely student density and share of rural population. However, these criteria are not sufficient to reflect full diversity of Ukrainian regions and local governments. There are some cases, where due to objective factors not accounted in the formula, the normative class size as determined by the formula is much larger than actual average class of secondary school managed by TG. This may be lack of good roads or bridges (which inhibits optimization of school network), or specific distribution of settlements where student live. These specific issues, on the basis of justified applications of local governments, may be resolved by allocation of additional funds from the reserve.

4. Problems created by delayed optimization of school network.

If local school network is not-optimal, then actual class sizes are lower than optimal, and the recurrent costs of the salaries of pedagogical staff may be significantly higher than received education subvention. The best course of action for the school founder is to optimize the school network. However, the optimization is politically difficult and takes time. For this reason, a reasonable solution may be an agreement of the school founder to adjust the local

network (to create satellite schools, to close some schools). In return for such commitment, the Ministry may allocate for one budget year some additional funds from the reserve.

At the same time, the allocation of the reserve should be a subject to strict conditions. The following conditions may be formulated:

- Documented efforts to optimize school network. Only school founders who consistently adjust the network of schools and classes to the changing number of students should be eligible for the funds from the reserve.
- Absence of remaining funds. Only school founders who have fully used their remaining funds of education subvention should be eligible for the funds from the reserve.

Of course, the above strategic uses of the reserve and necessary conditions are proposed to facilitate the discussion of Ukrainian experts. It would be good to involve also the national associations of local governments in these discussions.

4. Recommendations

On the basis of preceding discussion, and in line with the Polish model, the following recommendations regarding the legal regulation and use of the reserve of education subvention may be formulated:

- Use the reserve of education subvention for the same purposes as the subvention.

It is important that the reserve of education subvention is a real budgetary instrument of MES to support the same tasks for which education subvention was created. This means that the reserve should be spent on the salaries of pedagogical staff and should be spent during the budget year for which it was created. It should not be used as source of funds for higher education or for investment programs.

- Include the amount of the reserve in the budget laws.

Stating the amount of the reserve in the budget laws and advertising it in MES communication with the local governments and the general public will alert all interested that these funds are available and will motivate them to submit relevant applications. In this way, MES will be able to assess and satisfy the most urgent needs, and will receive important feedback regarding the functioning of the allocation of education subvention.

- Formulate in a legal act criteria for the allocation of the reserve.

It is very important that legitimate needs of local governments are recognized and satisfied during the budget years. This will prevent arrears in paying teacher salaries and will contribute to stability of Ukrainian education system. The criteria, consistent with the fact that education subvention may be used only for the salaries of pedagogical staff, should be defined in a legal act (possible criteria are proposed in section 3). The criteria for using the funds from the reserve should be publicly known, so that local governments know in which situations they may apply for these funds (and in which situations they cannot apply). These

criteria will also be used to assess received applications.

- Define in a legal act the procedure for allocation of funds from the reserve.

The procedure for allocation of funds from the reserve should be simple, transparent, just, and timely. The best approach is to invite applications from local governments as school founders in case they face problems. The detailed format of application, together with the required data, should be uniform for all applicants. The process of assessment of the applications, on the basis of criteria, should include representatives of national associations of local governments.

Hel, November 11, 2021

Annex. Legal acts used in the SN

Розпорядження Кабінету міністрів України від 18 грудня 2018 р. № 1012-р Київ Про розподіл резерву коштів освітньої субвенції з державного бюджету місцевим бюджетам у 2018 році

Розпорядження Кабінету міністрів України від 25 квітня 2018 р. № 282-р Київ Про перерозподіл деяких видатків державного бюджету, передбачених Міністерству освіти і науки на 2018 рік

Розпорядження Кабінету міністрів України від 05 вересня 2018 р. № 624-р Київ Про перерозподіл деяких видатків державного бюджету, передбачених Міністерству освіти і науки на 2018 рік

Розпорядження Кабінету міністрів України від 12 грудня 2018 р. № 965-р Київ Про перерозподіл деяких видатків державного бюджету, передбачених Міністерству освіти і науки на 2018 рік

Розпорядження Кабінету міністрів України від 27 листопада 2019 р. № 1106-р Київ Деякі питання використання у 2019 році освітньої субвенції з державного бюджету місцевим бюджетам

Розпорядження Кабінету міністрів України від 16 грудня 2020 р. № 1570-р Київ Про розподіл резерву коштів освітньої субвенції з державного бюджету місцевим бюджетам у 2020 році та перерозподіл деяких видатків державного бюджету, передбачених Міністерству освіти і науки на 2020 рік